OVERVIEW OF NET EARNINGS (EXCLUDING AAPT)

Telecom Corporation of New Zealand Limited and Subsidiaries

(in NZ$ millions, except percentages)	Year ended 30 June 1999	%	2000	%	Variation 00:99 $	%
Operating revenues						
Local service	**1,059**	*30.6*	**1,057**	*29.3*	**(2)**	*(0.2)*
Calling						
National	704	*20.4*	708	*19.7*	4	*0.6*
International	385	*11.1*	398	*11.0*	13	*3.4*
Other	51	*1.5*	50	*1.4*	(1)	*(2.0)*
	1,140	*33.0*	**1,156**	*32.1*	**16**	*1.4*
Interconnection	**71**	*2.1*	**86**	*2.4*	**15**	*21.1*
Cellular and other mobile	**502**	*14.5*	**546**	*15.2*	**44**	*8.8*
Data	**357**	*10.3*	**432**	*12.0*	**75**	*21.0*
Other operating revenues						
Directories	161	*4.7*	176	*4.9*	15	*9.3*
Equipment	109	*3.2*	84	*2.3*	(25)	*(22.9)*
Miscellaneous	57	*1.6*	64	*1.8*	7	*12.3*
	327	*9.5*	**324**	*9.0*	**(3)**	*(0.9)*
Total operating revenues (before abnormals)	**3,456**	*100.0*	**3,601**	*100.0*	**145**	*4.2*
Operating expenses						
Labour	467	*13.5*	406	*11.3*	(61)	*(13.1)*
Depreciation	551	*15.9*	556	*15.4*	5	*0.9*
Cost of sales	459	*13.3*	578	*16.1*	119	*25.9*
Other operating expenses	556	*16.1*	642	*17.8*	86	*15.5*
Total operating expenses (before abnormals)	**2,033**	*58.8*	**2,182**	*60.6*	**149**	*7.3*
Surplus from operations (before abnormals)	**1,423**	*41.2*	**1,419**	*39.4*	**(4)**	*(0.3)*
Net financing costs	(105)	*(3.0)*	(101)	*(2.8)*	4	*3.8*
Surplus from operations before income tax	**1,318**	*38.2*	**1,318**	*36.6*	**–**	–
Income tax expense	(420)	*(12.2)*	(413)	*(11.5)*	7	*1.7*
Surplus from operations after income tax	**898**	*26.0*	**905**	*25.1*	**7**	*0.8*
Abnormals	**1**	–	**–**	–	**(1)**	*(100.0)*
Surplus after income tax	**899**	*26.0*	**905**	*25.1*	**6**	*0.7*
Minority interests in profits of subsidiaries	(2)	–	(3)	*(0.1)*	(1)	*(50.0)*
Share of losses of associate company after income tax	(7)	*(0.2)*	(2)	–	5	*71.4*
Net Surplus	**890**	*25.8*	**900**	*25.0*	**10**	*1.1*
Capital note distribution costs after income tax	(55)	*(1.6)*	(54)	*(1.5)*	1	*1.8*
Net earnings attributable to shareholders	**835**	*24.2*	**846**	*23.5*	**11**	*1.3*

CONSOLIDATED STATEMENT OF FINANCIAL PERFORMANCE FOR THE YEAR ENDED 30 JUNE 2000

Telecom Corporation of New Zealand Limited and Subsidiaries

		Year ended 31 March		Three months ended 30 June	Year ended 30 June	
		1998	1999	1999	2000	2000
(Dollars in millions, except per share amounts)	notes	NZ$	NZ$	NZ$	NZ$	US$
Operating revenues						
Local service		1,025	1,058	264	1,064	499
Calling	2	1,242	1,161	270	1,488	698
Interconnection		56	65	20	90	42
Cellular and other mobile services		431	484	132	717	336
Data		305	342	96	535	251
Other operating revenues	2	339	324	66	437	205
Abnormal revenues	4	–	16	15	15	7
		3,398	3,450	863	4,346	2,038
Operating expenses						
Labour	3	494	479	112	486	228
Depreciation		564	553	136	583	273
Cost of sales		398	451	118	1,079	506
Other operating expenses	3	565	552	133	772	362
Abnormal expenses	4	37	15	22	–	–
		2,058	2,050	521	2,920	1,369
Surplus from continuing operations		**1,340**	**1,400**	**342**	**1,426**	**669**
Investment income	5	28	49	12	38	17
Interest expense	5	(155)	(159)	(34)	(218)	(102)
Surplus from continuing operations before income tax		**1,213**	**1,290**	**320**	**1,246**	**584**
Income tax expense	6	(397)	(411)	(98)	(395)	(185)
Surplus from continuing operations after income tax		**816**	**879**	**222**	**851**	**399**
Discontinued operations:	7					
Reversal of provision for loss on disposal of Pacific Star Group		30	–	–	–	–
Surplus after income tax		**846**	**879**	**222**	**851**	**399**
Share of losses of associate companies after income tax		–	–	(7)	(6)	(3)
Minority interests in profits of subsidiaries		–	(2)	–	(8)	(4)
Net surplus		**846**	**877**	**215**	**837**	**392**
Capital note distribution costs after income tax		(26)	(55)	(13)	(54)	(25)
Net earnings attributable to shareholders		**820**	**822**	**202**	**783**	**367**
Earnings per share from continuing operations		**$0.443**	**$0.469**	**$0.115**	**$0.447**	**$0.209**
Net earnings per share		**$0.459**	**$0.469**	**$0.115**	**$0.447**	**$0.209**
Weighted average number of ordinary shares outstanding (in millions)		1,786	1,752	1,753	1,753	1,753

Unaudited comparative information for the three months ended 30 June 1998 and the year ended 30 June 1999 is disclosed in Note 29 of these financial statements.

CONSOLIDATED STATEMENT OF MOVEMENTS IN CAPITAL FUNDS FOR THE YEAR ENDED 30 JUNE 2000

Telecom Corporation of New Zealand Limited and Subsidiaries

		Year ended 31 March		Three months ended 30 June	Year ended 30 June	
		1998	1999	1999	2000	2000
(Dollars in millions)	notes	NZ$	NZ$	NZ$	NZ$	US$
Capital funds at the beginning of the period		1,642	2,010	2,034	2,035	954
Net earnings attributable to shareholders		820	822	202	783	367
Movement in foreign currency translation reserve	18	1	–	1	48	23
Total recognised revenues and expenses for the period		821	822	203	831	390
Movement in minority interests		4	1	–	82	39
Dividends	18	(859)	(910)	(227)	(906)	(425)
Tax credit on supplementary dividends		103	104	25	100	47
Issue of capital notes	18	946	–	–	–	–
Discount on capital notes amortised		1	1	–	1	–
Redemption of capital notes		(6)	–	–	–	–
Capital contributed	18	2	6	–	19	9
Share repurchase	18	(644)	–	–	–	–
Capital funds at the end of the period		**2,010**	**2,034**	**2,035**	**2,162**	**1,014**
Represented by:						
Contributed capital		903	909	909	928	435
Foreign currency translation reserve		–	–	1	49	23
Minority interests		6	7	7	89	42
Retained earnings		160	176	176	153	72
Capital notes		941	942	942	943	442
		2,010	**2,034**	**2,035**	**2,162**	**1,014**

CONSOLIDATED STATEMENT OF FINANCIAL POSITION AS AT 30 JUNE 2000

Telecom Corporation of New Zealand Limited and Subsidiaries

(Dollars in millions)	notes	31 March 1999 NZ$	30 June 1999 NZ$	30 June 2000 NZ$	30 June 2000 US$
Assets					
Current assets:					
Cash		21	29	81	38
Short-term investments	8	673	114	617	289
Receivables and prepayments	9	754	691	918	431
Inventories	10	42	48	40	19
Total current assets		1,490	882	1,656	777
Long-term investments	11	47	530	455	213
Intangibles	12	58	56	1,620	760
Fixed assets	13	3,780	3,774	4,250	1,993
Total assets		**5,375**	**5,242**	**7,981**	**3,743**
Liabilities and Capital Funds					
Current liabilities:					
Bank overdraft		9	–	–	–
Accounts payable and accruals	14	801	821	1,242	583
Provisions – current	15	58	64	11	5
Debt due within one year	16	1,130	1,064	1,462	686
Provision for dividend	18	228	227	227	106
Total current liabilities		2,226	2,176	2,942	1,380
Deferred taxation	6	–	25	13	6
Provisions – non-current	15	3	3	3	1
Long-term debt	17	1,112	1,003	2,861	1,342
Total liabilities		3,341	3,207	5,819	2,729
Commitments and contingent liabilities	20,21				
Capital funds:	18				
Shareholders' funds		1,085	1,086	1,130	530
Capital notes		942	942	943	442
Minority interests		7	7	89	42
Total capital funds		2,034	2,035	2,162	1,014
Total liabilities and capital funds		**5,375**	**5,242**	**7,981**	**3,743**

On behalf of the Board

Roderick Deane

RODERICK DEANE, Chairman

THERESA GATTUNG, Chief Executive and Managing Director
Wellington, 10 August 2000

CONSOLIDATED STATEMENT OF CASH FLOWS FOR THE YEAR ENDED 30 JUNE 2000

Telecom Corporation of New Zealand Limited and Subsidiaries

		Year ended 31 March		Three months ended 30 June	Year ended 30 June	
		1998	1999	1999	2000	2000
(Dollars in millions)	note	NZ$	NZ$	NZ$	NZ$	US$
Cash flows from operating activities						
Cash was provided from/(applied to):						
Cash received from customers		3,285	3,423	872	4,192	1,966
Proceeds from cross border lease		-	-	15	-	-
Proceeds from liquidation of Executive Plan, net		-	16	-	-	-
Interest income		20	41	10	19	9
Dividend income		3	4	1	4	2
Payments to suppliers and employees		(1,273)	(1,380)	(399)	(2,093)	(981)
Restructuring, onerous contracts and Year 2000 payments		(60)	(65)	(16)	(58)	(27)
Income tax (paid)/refunded		(289)	(304)	51	(311)	(146)
Interest paid on debt		(149)	(161)	(41)	(208)	(98)
Net cash flows from operating activities	25	1,537	1,574	493	1,545	725
Cash flows from investing activities						
Cash was provided from/(applied to):						
Sale of fixed assets		11	21	1	57	27
(Purchase)/sale of short-term investments, net		(461)	(252)	560	(486)	(228)
Purchase of long-term investments		(8)	-	(104)	(238)	(112)
Proceeds from sale of subsidiary companies		-	16	-	95	45
Acquisition of AAPT Limited, excluding cash acquired		-	-	(385)	(1,189)	(558)
Purchase of fixed assets		(559)	(554)	(142)	(837)	(393)
Capitalised interest paid		(14)	(9)	(3)	(18)	(8)
Redemption of notes receivable		46	-	-	-	-
Net cash flows applied to investing activities		(985)	(778)	(73)	(2,616)	(1,227)
Cash flows from financing activities						
Cash was provided from/(applied to):						
Proceeds from long-term debt		269	12	9	1,850	867
Repayment of long-term debt		(191)	(199)	(49)	(246)	(115)
Proceeds/(repayment) of short-term debt, net		102	378	(135)	466	219
Capital contributed		2	6	-	23	11
Dividends paid		(841)	(914)	(228)	(894)	(420)
Capital note distribution costs paid		(26)	(79)	-	(77)	(36)
Share repurchase		(808)	-	-	-	-
Proceeds from issue of capital notes, net		940	-	-	-	-
Net cash flows from/(applied to) financing activities		(553)	(796)	(403)	1,122	526
Net cash flow		(1)	-	17	51	24
Foreign currency translation adjustment		-	-	-	1	-
Opening cash position (including bank overdrafts)		13	12	12	29	14
Closing cash position (including bank overdrafts)		12	12	29	81	38

STATEMENT OF FINANCIAL PERFORMANCE FOR THE YEAR ENDED 30 JUNE 2000

Telecom Corporation of New Zealand Limited

		Parent Company			
		Year ended 31 March 1999	Three months ended 30 June 1999	Year ended 30 June 2000	2000
(Dollars in millions)	notes	NZ$	NZ$	NZ$	US$
Operating revenues	2	806	202	822	386
Operating expenses		–	–	–	–
Surplus from operations		806	202	822	386
Investment income	5	37	11	104	48
Interest expense	5	(196)	(54)	(254)	(119)
Surplus before income tax		647	159	672	315
Income tax credit	6	52	15	50	24
Net earnings		**699**	**174**	**722**	**339**

STATEMENT OF MOVEMENTS IN CAPITAL FUNDS FOR THE YEAR ENDED 30 JUNE 2000

Telecom Corporation of New Zealand Limited

		Parent Company			
		Year ended 31 March 1999	Three months ended 30 June 1999	Year ended 30 June 2000	2000
(Dollars in millions)	note	NZ$	NZ$	NZ$	US$
Capital funds at the beginning of the period		795	694	666	312
Net earnings		699	174	722	339
		1,494	868	1,388	651
Dividends	18	(910)	(227)	(906)	(425)
Tax credit on supplementary dividends	18	104	25	100	47
Capital contributed	18	6	–	19	9
Capital funds at the end of the period		**694**	**666**	**601**	**282**
Represented by:					
Contributed capital		909	909	928	435
Retained earnings		(215)	(243)	(327)	(153)
		694	**666**	**601**	**282**

STATEMENT OF FINANCIAL POSITION AS AT 30 JUNE 2000

Telecom Corporation of New Zealand Limited

		Parent Company			
		31 March 1999	30 June 1999	30 June 2000	30 June 2000
(Dollars in millions)	notes	NZ$	NZ$	NZ$	US$
Assets					
Current assets:					
Prepaid income tax	6	1	65	6	3
Accounts receivable		–	–	2	1
Total current assets		1	65	8	4
Future tax benefit	6	26	–	25	12
Investments	11	3,830	3,381	5,033	2,360
Total assets		**3,857**	**3,446**	**5,066**	**2,376**
Liabilities and Capital Funds					
Current liabilities:					
Accounts payable and accruals	14	31	30	18	9
Provision for dividend	18	228	227	227	106
Due to subsidiary companies	22	2,904	2,523	4,220	1,979
Total current liabilities		3,163	2,780	4,465	2,094
Commitments and contingent liabilities	20,21				
Capital funds:	18				
Shareholders' funds		694	666	601	282
Total liabilities and capital funds		**3,857**	**3,446**	**5,066**	**2,376**

On behalf of the Board

Roderick Deane

RODERICK DEANE, Chairman

THERESA GATTUNG, Chief Executive and Managing Director
Wellington, 10 August 2000

STATEMENT OF CASH FLOWS FOR THE YEAR ENDED 30 JUNE 2000

Telecom Corporation of New Zealand Limited

		Parent Company			
		Year ended 31 March	Three months ended 30 June	Year ended 30 June	
		1999	1999	2000	2000
(Dollars in millions)	note	NZ$	NZ$	NZ$	US$
Cash flows from operating activities					
Cash was provided from/(applied to):					
Interest income		37	11	104	49
Dividends received from subsidiary companies		825	202	808	379
Interest paid on debt		(196)	(54)	(253)	(119)
Net cash flows from operating activities	25	666	159	659	309
Cash flows from investing activities					
Cash was provided from/(applied to):					
Advances from subsidiary companies, net		232	558	735	345
Redemption/(purchase) of investments, net		11	(490)	(507)	(238)
Net cash flows from investing activities		243	68	228	107
Cash flows from financing activities					
Cash was provided from/(applied to):					
Dividends paid		(914)	(227)	(891)	(418)
Repayment of short-term debt		(1)	–	–	–
Capital contributed		6	–	4	2
Net cash flows applied to financing activities		(909)	(227)	(887)	(416)
Net cash flow		–	–	–	–
Opening cash position		–	–	–	–
Closing cash position		–	–	–	–

NOTE 1 STATEMENT OF ACCOUNTING POLICIES

Reporting Entity and Statutory Base
Telecom Corporation of New Zealand Limited is a company registered in New Zealand under the Companies Act 1993, and is an issuer for the purposes of the Financial Reporting Act 1993.

The financial statements presented are those of Telecom Corporation of New Zealand Limited (the "Company" or the "Parent Company") its subsidiaries and associates (the "Telecom Group" or "Telecom").

Nature of Operations
Telecom is a major supplier of telecommunications services in New Zealand and Australia. Telecom provides a full range of telecommunications products and services including local, national, international and value-added telephone services, cellular and other mobile services, data and Internet services, equipment sales and installation services, leased services and directories.

Basis of Preparation
The financial statements have been prepared in accordance with the Financial Reporting Act 1993 which requires compliance with accounting practice generally accepted in New Zealand ("NZ GAAP"). This differs in certain significant respects from accounting practice generally accepted in the United States ("US GAAP"). For a description of the significant differences and related effect on these financial statements, see Note 30.

The financial statements are expressed in New Zealand dollars. The amounts pertaining to the most recent financial period are also expressed in United States ("US") dollars, the latter being presented solely for convenience and translated from New Zealand dollars, as a matter of arithmetical computation only, at a rate on 30 June 2000 of NZ$1.00 to US$0.4690. The US dollar amounts should not be construed as representations that the New Zealand dollars have been, could be, or could in the future be converted into US dollars at this or any other rate. References in these financial statements to "$" and "NZ$" are to New Zealand dollars, references to "US$" are to US dollars and references to "A$" are to Australian dollars.

Measurement Basis
The measurement basis adopted in the preparation of these financial statements is historical cost, modified by the revaluation of certain investments as identified in specific accounting policies below.

Specific Accounting Policies

Basis of Consolidation

Subsidiaries
Subsidiaries are those entities controlled, directly or indirectly, by the Telecom Group.

The consolidated financial statements are prepared from the accounts of the Company and its wholly and majority-owned subsidiaries using the purchase method of consolidation. All significant intercompany accounts and transactions are eliminated on consolidation.

Associates
Associates are entities in which the Telecom Group has significant influence, but not control, over the operating and financial policies.

Associate companies are reflected in the consolidated financial statements using the equity method whereby Telecom's share of the results of associates is included in consolidated net earnings attributable to shareholders.

Where the equity accounted carrying amount of an investment in an entity falls below zero, the equity method of accounting is suspended and the investment recorded at zero. If this occurs, the equity method of accounting is not resumed until such time as the Telecom Group's share of losses and reserve decrements, not recognised during the financial years in which the equity method was suspended, are offset by the current share of profits and reserves.

Goodwill Arising on Acquisition
Goodwill represents the excess of purchase consideration over the fair value of net assets acquired at the time of acquisition of a business or shares in a subsidiary or associate. Goodwill is amortised on a systematic basis over the period benefits are expected to arise, which will be no more than 20 years.

Acquisition or Disposal During the Year
Where an entity becomes or ceases to be a Telecom Group entity during the year, the results of that entity are included in the net earnings of the Telecom Group from the date that control or significant influence commenced or until the date that control or significant influence ceased.

Revenue Recognition
Telecom generally recognises revenues as it provides services or delivers products to customers. Billings for telecommunications services are made on a monthly basis throughout the month. Unbilled revenues from the billing cycle date to the end of each month are recognised as revenue during the month the service is provided. Revenue recognition is deferred in respect of the portion of fixed monthly charges that have been billed in advance.

Accounts Receivable
Accounts receivable are recorded at expected realisable value after providing for bad and doubtful accounts expected to arise in subsequent accounting periods.

Bad debts are written off against the provision for doubtful accounts in the period in which it is determined that the debts are uncollectable.

Inventories
Inventories principally comprise materials for self-constructed network assets, critical maintenance spares, customer premises equipment held for rental or sale and mobile equipment held for sale. Inventories are stated at the lower of cost and net realisable value after due consideration for excess and obsolete items. Cost is determined on a first-in first-out or weighted average cost basis.

Investments
Long-term investments are stated at cost. Long-term investments include the Company's investment in subsidiaries.

Investments in associate companies are stated at the Company's share of the fair value of the net tangible assets at acquisition plus the share of post-acquisition movements in reserves.

Investments not expected to be held to maturity are stated at market value, with the resulting gains or losses taken to earnings.

Where, in the opinion of the Directors, there has been a permanent diminution in the value of investments this is recognised in the current period.

Fixed Assets
Fixed assets are valued as follows:

- The value of fixed assets purchased from the Government was determined on the basis of depreciated replacement cost using estimated remaining lives as at 1 April 1987.
- Subsequent additions are valued at cost. The cost of additions to plant and equipment and other fixed assets constructed by Telecom consists of all appropriate costs of development, construction and installation, comprising material, labour, direct overhead and transport costs.

NOTE 1 **Statement of Accounting Policies** (continued)

- For each fixed asset project, interest costs incurred during the period required to complete and prepare the fixed asset for its intended use are capitalised as part of the total cost.

Software Developed for Internal Use

Telecom capitalises the direct costs associated with the development of network and business software for internal use where project success is regarded as probable. Capitalised costs include external direct costs of materials and services consumed, payroll and direct payroll-related costs for employees (including contractors) directly associated with the project and interest costs incurred while developing the software. Software developed for internal use is depreciated over its useful life to the Telecom Group.

Depreciation

Depreciation is charged on a straight-line basis to write down the cost of the fixed assets to their estimated residual value over their estimated useful lives, which are as follows:

Telecommunications equipment and plant:	
Customer local access	3-50 years
Junctions and trunk transmission systems	10-50 years
Switching equipment	3-15 years
Customer premises equipment	3-5 years
Other network equipment	4-15 years
Buildings	40-50 years
Motor vehicles	4-10 years
Furniture and fittings	5-10 years
Computer equipment	3-5 years

Where the remaining useful lives or recoverable values have diminished due to technological change or market conditions, depreciation is accelerated or the assets are written down.

Land and capital work in progress are not depreciated.

Where a fixed asset is disposed of, the profit or loss recognised in the Statement of Financial Performance is calculated as the difference between the sale price and the carrying value of the fixed asset.

Leased Assets

Telecom is a lessor of customer premises equipment. Such leases are considered operating leases because substantially all the benefits and risks of ownership remain with Telecom. Rental income is taken to revenue on a monthly basis in accordance with the lease term.

Telecom is a lessee of certain plant, equipment, land and buildings under both operating and finance leases. Lease costs relating to operating leases are charged against earnings as incurred. Finance leases, which effectively transfer to Telecom substantially all the risks and benefits of ownership of the leased assets, are capitalised at the present value of the minimum lease payments. The leased assets and corresponding liabilities are disclosed and the leased assets are depreciated over the period Telecom is expected to benefit from their use.

Spectrum Licences

Costs incurred on the acquisition of spectrum licences are amortised from the date the underlying asset is held ready for use on a straight-line basis over the period of their expected benefit, which does not exceed fifteen years.

Debt

Debt is stated at face value less unamortised discounts, premiums and prepaid interest. Discounts, premiums and prepaid interest are amortised to interest expense on a yield to maturity basis over the period of the borrowing. Borrowing costs such as origination, commitment and transaction fees are deferred and amortised over the period of the borrowing.

Compensated Absences

The liability for employees' compensation for future absences, calculated on an actuarial basis, is accrued in respect of employees' services already rendered and where the obligation relates to rights that may eventually vest.

Research and Development Costs

Research and development costs are charged to earnings as incurred, except where, in the case of development costs, future benefits are expected beyond any reasonable doubt to exceed these costs. Where development costs are deferred, they are amortised over future periods on a basis related to the expected future benefits.

Taxation

The taxation expense charged to earnings includes both current and deferred tax and is calculated after allowing for permanent differences.

Deferred taxation calculated on a partial basis using the liability method is accounted for on timing differences between the earnings stated in the financial statements and the assessable income computed for taxation purposes. Deferred taxation is recognised only on those timing differences that are expected to crystallise within the foreseeable future.

Foreign Currency

Transactions

Transactions denominated in a foreign currency are converted at the New Zealand exchange rate at the date of the transaction. Foreign currency receivables and payables at balance date are translated at exchange rates current at balance date. Exchange differences arising on the translation of accounts payable and receivable in foreign currencies are recognised in the Statement of Financial Performance.

Exchange gains and losses and hedging costs arising on contracts entered into as hedges of firm commitments are deferred until the date of such transactions at which time they are included in the determination of net earnings.

Where capital project commitments are hedged against foreign currency rate risk, the exchange difference on the hedging transaction up to the date of purchase and all other costs associated with the hedging transaction are capitalised.

All exchange gains and losses relating to other hedge transactions are brought to account in the Statement of Financial Performance in the same period as the exchange differences on the items covered by the hedge transactions. Costs on such contracts are amortised over the life of the hedge contract.

Translation of Foreign Group Entities

Assets and liabilities of independent overseas subsidiaries are translated at exchange rates existing at balance date. The revenues and expenses of these entities are translated at rates approximating the exchange rates ruling at the dates of the transactions. The exchange gain or loss arising on translation is carried directly to a foreign currency translation reserve.

Derivative Financial Instruments

Telecom uses derivative financial instruments to reduce its exposure to fluctuations in foreign currency exchange rates and interest rates.

Telecom does not currently hold or issue derivative financial instruments for trading purposes. Gains and losses on derivatives are accounted for on the same basis as the underlying physical exposures. Accordingly, hedge gains and losses are included in the Statement of Financial Performance when the gains or losses arising on the related physical exposures are recognised in the Statement of Financial Performance.

NOTE 1 **Statement of Accounting Policies** (continued)

For an instrument to qualify as a hedge, it must be effective at reducing the risk associated with the exposure being hedged and must be designated as a hedge at the inception of the contract.

Derivative financial instruments that do not qualify or no longer qualify as hedges are stated at market values and any resultant gain or loss is recognised in the Statement of Financial Performance.

Interest rate swaps and cross currency interest rate swaps that hedge an underlying physical exposure are accounted for using the accrual method of accounting. Interest receivable and payable under the terms of the interest rate swaps and cross currency interest rate swaps are accrued over the period to which the payments or receipts relate, and are treated as an adjustment to interest expense or capital note distribution costs.

The foreign exchange gains and losses on the principal value of cross currency swaps are reflected in the Statement of Financial Performance using the spot rate which offsets the foreign exchange gains and losses recorded on the underlying hedged transaction.

Premiums paid for interest rate options and the net settlement on maturity of forward rate agreements are amortised over the life of the underlying hedged item.

Forward exchange contracts are accounted for as outlined in the accounting policy for foreign currency transactions.

Cash flows from derivatives are recognised in the Statement of Cash Flows in the same category as that of the hedged item.

Cash and Cash Equivalents

For the purposes of the Statement of Cash Flows, cash and cash equivalents are considered to be cash on hand and in banks, net of bank overdrafts. Cash flows from certain items are disclosed net, due to the short-term maturities and volume of transactions involved.

Earnings Per Share

Earnings per share is computed by dividing net earnings by the weighted average number of ordinary shares outstanding during each period.

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Annual Balance Date Change

Effective 1 April 1999, the Company changed its annual balance date from 31 March to 30 June. These financial statements include the transition period result for the three months ended 30 June 1999.

Reclassifications

Certain reclassifications of prior periods' data have been made to conform to current year classifications.

Changes in Accounting Policies

The accounting policies used in the preparation of the financial statements for the year ended 30 June 2000 are consistent with those used in the preparation of the published financial statements for the three month transition period ended 30 June 1999 and the year ended 31 March 1999.

NOTE 2 **CALLING AND OTHER OPERATING REVENUES**

	Telecom Group			
	Year ended 31 March		Three months ended 30 June	Year ended 30 June
	1998	1999	1999	2000
(Dollars in millions)	NZ$	NZ$	NZ$	NZ$
Calling				
National	732	709	171	932
International	450	400	88	506
Other	60	52	11	50
	1,242	**1,161**	**270**	**1,488**
Other operating revenues				
Directories	147	160	19	176
Equipment revenue	144	109	28	84
Miscellaneous other services	48	55	19	177
	339	**324**	**66**	**437**

Parent Company

Operating revenues principally comprise dividends received from subsidiary companies.

NOTE 3 OPERATING EXPENSES

Labour

Included in labour costs are pension contributions of $3 million to the Government Superannuation Fund (30 June 1999: $1 million, 31 March 1999: $4 million, 31 March 1998: $5 million) and $5 million on behalf of Australian employees as required by the Superannuation Guarantee (Administration) Act 1992. Telecom has no other obligations to provide pension benefits in respect of present employees. Telecom currently pays administration and management fees, insurance premiums and other expenses incurred with respect to employees' membership of the Telecom Retirement Savings Plan, but only members contribute to that plan.

	Telecom Group			
	Year ended 31 March		Three months ended 30 June	Year ended 30 June
	1998	1999	1999	2000
(Dollars in millions)	NZ$	NZ$	NZ$	NZ$
Other Operating Expenses				
Other operating expenses include:				
Lease and rental costs	35	33	8	42
Research and development costs	6	10	1	5
Foreign exchange (gains)/losses	(4)	1	-	(4)
Goodwill amortised	4	7	2	43
Bad debts written off	33	25	5	40
Increase in provision for doubtful accounts	1	2	–	7
Provision for inventory obsolescence	2	2	–	2
Loss on disposal of fixed assets	4	5	–	7
Auditors' remuneration:				
Audit fees paid to principal auditors	1	1	–	1
Fees paid for other services provided by principal auditors	3	3	1	3
Directors' fees	1	1	–	1

NOTE 4 ABNORMAL ITEMS

	Telecom Group			
	Year ended 31 March		Three months ended 30 June	Year ended 30 June
	1998	1999	1999	2000
(Dollars in millions)	NZ$	NZ$	NZ$	NZ$
Abnormal Revenues				
Sale of AAPT Sat-Tel Pty Limited	–	–	–	15
Cross border lease	–	–	15	–
Liquidation of the Executive Share Ownership Plan	–	16	–	–
	–	**16**	**15**	**15**
Abnormal Expenses				
Onerous contract buy-out costs	–	–	22	–
Restructuring costs	–	15	–	–
Discontinuance of HFC roll-out & closure of First Media Limited	37	–	–	–
	37	**15**	**22**	**–**

Abnormal Revenues

Sale of AAPT Sat-Tel Pty Limited

In March 2000, AAPT Limited ("AAPT") completed the sale of its wholly owned subsidiary AAPT Sat-Tel Pty Limited to New Skies Networks Australia Pty Limited. Included in the Consolidated Statement of Financial Performance are post acquisition profits relating to this sale, before minority interests, of $15 million.

Cross Border Lease

During the three months ended 30 June 1999, a gain of $15 million was recognised on the prepayment of Telecom's scheduled payment obligations relating to a cross border finance lease.

Liquidation of the Executive Share Ownership Plan (the "Executive Plan")

The liquidation of the Executive Plan was completed in March 1999. The Trustee of the Executive Plan had disposed of the 1.9 million unallocated shares held on trust and remitted the net proceeds to Telecom as the residuary beneficiary. The net proceeds received were $16 million.

Abnormal Expenses

Onerous Contract Buy-out Costs

During the three months ended 30 June 1999, the costs of buying out the terms of certain onerous contracts were identified and provided for. The contracts were onerous as the unavoidable costs of meeting the contractual obligations exceeded their economic benefits.

NOTE 4 **Abnormal Items** (continued)

Restructuring
During the year ended 31 March 1999, Telecom reached an agreement with specialist call centre operator SITEL Asia Pacific to contract out the provision of operator services. The decision to outsource operator services resulted in approximately 560 redundancies at a cost of $15 million.

Discontinuance of HFC Roll-out & Closure of First Media Limited ("First Media")
During the year ended 31 March 1998, Telecom identified and provided for the estimated costs associated with the termination of the residential hybrid fibre/coax cable roll-out and the closure of First Media, a cable television operator.

NOTE 5 **INVESTMENT INCOME/INTEREST EXPENSE**

	Telecom Group			
	Year ended 31 March		Three months ended 30 June	Year ended 30 June
	1998	1999	1999	2000
(Dollars in millions)	NZ$	NZ$	NZ$	NZ$
Investment income:				
Interest received	25	45	11	34
Dividends received	3	4	1	4
Total investment income	**28**	**49**	**12**	**38**
Interest expense:				
Fixed loans	113	110	23	108
Finance leases	6	5	1	2
Other interest	50	53	13	126
	169	168	37	236
Less interest capitalised	(14)	(9)	(3)	(18)
Total interest expense	**155**	**159**	**34**	**218**

Parent Company
Investment income and interest expense comprise interest received from and paid to subsidiary companies.

NOTE 6 **INCOME TAX**

The income tax expense/(credit) is determined as follows:

	Telecom Group				Parent Company		
	Year ended 31 March		Three months ended 30 June	Year ended 30 June	Year ended 31 March	Three months ended 30 June	Year ended 30 June
	1998	1999	1999	2000	1999	1999	2000
(Dollars in millions)	NZ$	NZ$	NZ$	NZ$	NZ$	NZ$	NZ$
Surplus from continuing operations before income tax	1,213	1,290	320	1,246	647	159	672
Tax at current rate of 33%	400	426	106	411	214	52	222
Adjustments to taxation for permanent differences:							
Intercompany dividends	–	–	–	–	(266)	(67)	(267)
Other	(3)	(15)	(8)	(16)	–	–	(5)
Total income tax expense/(credit)	**397**	**411**	**98**	**395**	**(52)**	**(15)**	**(50)**
The income tax expense/(credit) is represented by:							
Current taxation	399	388	99	348	(52)	(15)	(50)
Deferred taxation	(2)	23	(1)	47	–	–	–
	397	411	98	395	(52)	(15)	(50)
Deferred income tax expense/(credit) results from the following:							
Depreciation	15	9	(1)	32	–	–	–
Provisions, accruals and other	(36)	7	(5)	(1)	–	–	–
Year 2000 expenditure	4	3	2	8	–	–	–
Tax losses in overseas subsidiary company	–	–	–	1	–	–	–
Restructuring provisions	15	4	3	7	–	–	–
	(2)	23	(1)	47	–	–	–

NOTE 6 **Income Tax** (continued)

The Statement of Financial Position balances are:

	Telecom Group			Parent Company		
	31 March	30 June		31 March	30 June	
	1999	1999	2000	1999	1999	2000
(Dollars in millions)	NZ$	NZ$	NZ$	NZ$	NZ$	NZ$
Current taxation:						
Balance at the beginning of the year	17	71	(23)	1	1	65
Total taxation (expense)/credit in the current year	(388)	(99)	(348)	52	15	50
Tax benefit of capital note distribution costs	28	7	27	–	–	–
Tax paid/(refunded)	304	(51)	311	–	–	–
Supplementary dividend tax credit						
– previous year fourth quarter interim and special	27	26	–	27	26	–
– first, second and third quarter interims	78	–	75	78	–	75
– transition period interim	–	25	–	–	25	–
Tax loss offset with subsidiary companies	–	–	–	(52)	–	(59)
Supplementary dividend tax credit offset with subsidiary companies	–	–	–	(105)	–	(126)
Transfer from deferred taxation	–	–	(18)	–	–	–
Other	5	(2)	(1)	–	(2)	1
Prepaid income tax/(income tax payable) (see Notes 9 and 14)	71	(23)	23	1	65	6
Deferred taxation:						
Balance at the beginning of the year	23	–	(25)	27	26	–
Provided in the current year	(23)	1	(47)	–	–	–
Supplementary dividend tax credit						
– previous year fourth quarter interim and special	(27)	(26)	–	(27)	(26)	–
– current year fourth quarter interim	26	–	25	26	–	25
Transfer to current taxation	–	–	18	–	–	–
Balance on acquisition of subsidiary company	–	–	14	–	–	–
Other	1	–	2	–	–	–
(Deferred taxation)/future tax benefit	**–**	**(25)**	**(13)**	**26**	**–**	**25**
Deferred taxation balances consist of the following:						
Depreciation	(93)	(92)	(128)	–	–	–
Provisions, accruals and other	34	39	45	–	–	–
Year 2000 expenditure	21	19	11	–	–	–
Restructuring provisions	12	9	2	–	–	–
Tax losses in overseas subsidiary company	–	–	32	–	–	–
Supplementary dividend tax credit	26	–	25	26	–	25
	–	(25)	(13)	26	–	25

At 30 June 2000, a deferred tax asset of $7 million (30 June 1999: $6 million, 31 March 1999: $6 million), in respect of timing differences relating to depreciation on buildings, has not been recognised.

In accordance with the Income Tax Act 1994, Telecom received tax credits from the Inland Revenue Department equivalent to the supplementary dividends paid. Included as a deferred tax asset is $25 million representing a tax credit due on the payment of supplementary dividends that will be paid in conjunction with the fourth quarter dividend.

AAPT has not recognised in its deferred taxation balance the tax effect of accumulated losses amounting to A$7 million (based on the Australian corporation tax rate of 34%). Obtaining the benefits of these tax losses is dependent upon deriving sufficient assessable income, meeting conditions for deductibility and complying with Australian tax legislation.

NOTE 7 DISCONTINUED OPERATIONS

Telecom announced on 22 July 1996 that it was reviewing the operations of those of its Australian subsidiaries which formed the Pacific Star Group ("Pacific Star") at which time a formal plan of disposal or wind-down of the Pacific Star businesses was approved by the Board.

The winding down of Pacific Star operations progressed satisfactorily resulting in a reduction in the provision for loss on disposal of Pacific Star by $30 million at 31 March 1998. The process of winding down the discontinued Pacific Star operations was completed during the year ended 30 June 2000.

NOTE 8 SHORT-TERM INVESTMENTS

	Telecom Group		
	31 March 1999	30 June 1999	30 June 2000
(Dollars in millions)	NZ$	NZ$	NZ$
Short-term deposits	47	55	301
Government securities	15	3	9
Other money market securities	611	56	50
Associate company advance (see Note 22)	–	–	257
	673	**114**	**617**

NOTE 9 RECEIVABLES AND PREPAYMENTS

	Telecom Group		
	31 March 1999	30 June 1999	30 June 2000
(Dollars in millions)	NZ$	NZ$	NZ$
Trade receivables	499	515	742
Less allowance for doubtful accounts	(22)	(23)	(57)
	477	492	685
Unbilled rentals and tolls	163	119	159
Prepaid income tax (see Note 6)	71	–	23
Prepaid expenses and other receivables	43	80	51
	754	**691**	**918**

NOTE 10 INVENTORIES

	Telecom Group		
	31 March 1999	30 June 1999	30 June 2000
(Dollars in millions)	NZ$	NZ$	NZ$
Maintenance materials and consumables	7	5	–
Goods held for resale	11	11	16
Revenue work in progress	14	20	14
Materials for self-constructed assets	21	23	24
	53	59	54
Less provision for inventory obsolescence	(11)	(11)	(14)
	42	**48**	**40**

NOTE 11 **LONG-TERM INVESTMENTS**

	Telecom Group			Parent Company		
	31 March 1999	30 June 1999	30 June 2000	31 March 1999	30 June 1999	30 June 2000
(Dollars in millions)	NZ$	NZ$	NZ$	NZ$	NZ$	NZ$
Term deposits	26	26	34	–	–	–
International telecommunications investments	21	21	21	–	–	–
Associate companies:						
Investments (refer below)	–	(7)	30	–	–	–
Advances	–	104	158	–	–	–
Shares in listed companies	–	386	166	–	–	166
Other long-term investments	–	–	46	–	–	–
Subsidiary companies (see Note 23):						
Shares	–	–	–	2,324	2,814	3,156
Term loans, net	–	–	–	1,506	567	1,711
	47	**530**	**455**	**3,830**	**3,381**	**5,033**

Associate Company Investments

	Telecom Group		
	31 March 1999	30 June 1999	30 June 2000
(Dollars in millions)	NZ$	NZ$	NZ$
Cost of investment in associates	–	–	45
Opening balance of share of associates' equity	–	–	(7)
Share of associates' deficit	–	(7)	(6)
Net exchange difference on translation of associate	–	–	(2)
Equity accounted value of the investment	–	(7)	30

Shares in Listed Companies

During the year ended 30 June 2000, Telecom purchased a 10% stake in Independent Newspapers Limited ("INL") and a 2% stake in eVentures Limited ("eVentures"). At 30 June 2000 the market values of Telecom's investments in INL and eVentures were $155 million and $3 million respectively.

During the three months ended 30 June 1999, Telecom purchased a 19.7% stake in AAPT. At 30 June 1999 the market value of Telecom's investment in AAPT was NZ$337 million. On 27 November 1999 Telecom purchased an additional 61.7% shareholding in AAPT, bringing the total shareholding at that date to 81.4%.

NOTE 12 **INTANGIBLES**

	Telecom Group		
	31 March 1999	30 June 1999	30 June 2000
(Dollars in millions)	NZ$	NZ$	NZ$
Goodwill	58	56	1,469
Spectrum licences	–	–	151
	58	**56**	**1,620**

NOTE 13 FIXED ASSETS

	Telecom Group					
	Tele-communications equipment	Capital work in progress	Freehold land	Buildings	Other fixed assets	TOTAL
(Dollars in millions)	NZ$	NZ$	NZ$	NZ$	NZ$	NZ$
Cost	7,554	398	111	525	830	9,418
Less accumulated depreciation	(4,288)	–	–	(243)	(637)	(5,168)
Net book value at 30 June 2000	**3,266**	**398**	**111**	**282**	**193**	**4,250**
Cost	6,798	184	112	517	892	8,503
Less accumulated depreciation	(3,837)	–	–	(225)	(667)	(4,729)
Net book value at 30 June 1999	**2,961**	**184**	**112**	**292**	**225**	**3,774**
Cost	6,693	187	111	516	878	8,385
Less accumulated depreciation	(3,737)	–	–	(222)	(646)	(4,605)
Net book value at 31 March 1999	**2,956**	**187**	**111**	**294**	**232**	**3,780**

Values Ascribed to Land and Buildings

Telecom's properties consist primarily of special-purpose network buildings, which form an integral part of the telecommunications network. The Directors estimate that the fair valuation of land and buildings (excluding properties designated for disposal) is approximately equivalent to their net book value as at 30 June 2000, taking into account their integral value to the network.

Included in land and buildings at 30 June 2000 are properties held for sale at their estimated realisable value of $11 million (30 June 1999: $13 million, 31 March 1999: $12 million).

Operating Leases

Included in telecommunications equipment at 30 June 2000 is equipment (principally customer premises equipment) leased to customers under operating leases with a cost of $303 million (30 June 1999: $284 million, 31 March 1999: $282 million) together with accumulated depreciation of $272 million (30 June 1999: $262 million, 31 March 1999: $260 million).

Included in buildings at 30 June 2000 are buildings on leasehold land with a cost of $11 million (30 June 1999: $9 million, 31 March 1999: $9 million) together with accumulated depreciation of $2 million (30 June 1999: $2 million, 31 March 1999: $2 million).

Finance Leases

Included in telecommunications equipment at 30 June 2000 are assets capitalised under finance leases with a cost of $541 million (30 June 1999: $576 million, 31 March 1999: $287 million) together with accumulated depreciation of $391 million (30 June 1999: $376 million, 31 March 1999: $204 million).

Land Claims

Under the Treaty of Waitangi Act 1975, all interests in land included in the assets purchased from the New Zealand Government may be subject to claims to the Waitangi Tribunal, which has the power to recommend, in appropriate circumstances, with binding effect, that the land be resumed by the Government in order that it be returned to Maori claimants. In the event that the Government resumes land, compensation will be paid to Telecom under the provisions of the Public Works Act 1981. If this is insufficient to cover the loss, certain additional compensation is payable under the provisions of the Sale and Purchase Agreement between the Company and the Government.

Under the State Owned Enterprises Act 1986, the Governor General of New Zealand, if satisfied that any land or interest in land held by Telecom is Wahi Tapu (being land of special spiritual, cultural or historical tribal significance), may declare by Order in Council that the land be resumed by the Government, with compensation payable to Telecom under the provisions of the Public Works Act 1981. Telecom would expect to negotiate with the new Maori owners for continued occupancy rights of any sites resumed by the Government.

NOTE 14 ACCOUNTS PAYABLE AND ACCRUALS

	Telecom Group		
	31 March	30 June	
	1999	1999	2000
(Dollars in millions)	NZ$	NZ$	NZ$
Trade accounts payable	502	520	969
Accrued personnel costs	69	60	66
Rentals billed in advance	56	55	64
Accrued interest	60	75	91
Income tax payable (see Note 6)	-	23	-
Other accrued expenses	114	88	52
	801	**821**	**1,242**

Parent Company
Accounts payable and accruals comprise non-resident withholding tax and other sundry payable balances.

NOTE 15 PROVISIONS – ONEROUS CONTRACTS, RESTRUCTURING AND YEAR 2000

	Telecom Group		
	31 March	30 June	
	1999	1999	2000
(Dollars in millions)	NZ$	NZ$	NZ$
Current:			
Onerous contracts provision	-	22	8
Restructuring provisions	34	25	3
Year 2000 provision	24	17	-
	58	**64**	**11**
Non-current:			
Restructuring provisions	**3**	**3**	**3**

Onerous Contracts
During the three months ended 30 June 1999, estimated costs of $22 million to buy-out the terms of certain onerous contracts were identified and provided for. During the year ended 30 June 2000 costs of $14 million were charged against this provision.

Restructuring
A strategic restructuring of Telecom was announced towards the end of the 1993 financial year. It was estimated that the cost of implementing this restructuring would be $450 million. This was provided for in the fourth quarter earnings of the year ended 31 March 1993 as an abnormal restructuring cost. During the year ended 30 June 2000, costs of $5 million were charged against this provision. As at 30 June 2000, the balance of this provision was $6 million (30 June 1999: $11 million, 31 March 1999: $12 million), the majority of which relates to expected losses on disposal of surplus freehold properties.

A strategic restructuring, aimed at improving service and reducing operating costs, was finalised in the fourth quarter of the 1997 financial year. In addition, restructuring costs arising out of the Performance 2000 project, aimed at substantially reducing Telecom's operating costs, had been identified as at 31 March 1997. All of these restructuring costs, amounting to $65 million, were provided for in the fourth quarter results of the year ended 31 March 1997. During the year ended 30 June 2000, redundancy and other restructuring costs of $17 million were charged against this provision. As at 30 June 2000, the balance of this provision was nil (30 June 1999: $17 million, 31 March 1999: $18 million).

Redundancy costs of $15 million resulting from the outsourcing of operator services were identified and provided for during the year ended 31 March 1999. The remaining balance of this provision (31 March 1999: $7 million) was paid out during the three months to 30 June 1999.

Year 2000
The operating costs of making the modifications necessary to maintain functionality into the year 2000 and beyond was estimated at $87 million and a provision raised at 31 March 1997. This provision had been fully utilised by 30 June 2000.

NOTE 16 DEBT DUE WITHIN ONE YEAR

	Telecom Group		
	31 March 1999	30 June 1999	30 June 2000
(Dollars in millions)	NZ$	NZ$	NZ$
Long-term debt maturing within one year (see Note 17):			
Bonds and other loans	159	229	130
Finance leases	18	18	58
	177	247	188
Short-term debt:			
Commercial paper	692	545	789
Notes	260	263	485
Other loans	1	9	–
	953	817	1,274
	1,130	**1,064**	**1,462**

The weighted average interest rates at 30 June 2000 (inclusive of the effects of hedging) were 6.20% for commercial paper and 6.73% for notes (30 June 1999: 4.56% and 4.65%, 31 March 1999: 4.45% and 4.33% respectively).

Commercial paper comprises amounts issued under Telecom's US$750 million European Commercial Paper Programme and Telecom's $200 million Asian Commercial Paper Programme. Issues outstanding at 30 June 2000 are denominated in NZ dollars, US dollars, Swiss francs and Euros and are stated inclusive of the effect of hedging transactions.

Notes comprise amounts issued under Telecom's $500 million note facility.

As at 30 June 2000 Telecom had a committed stand-by credit facility of $1,600 million with the major New Zealand trading banks (this facility was cancelled on 31 July 2000), and access to US$200 million of committed short-term funding through a standby facility. Telecom also had committed overdraft facilities of $20 million with New Zealand banks. In addition AAPT had access to an undrawn committed facility with a major Australian trading bank of A$60 million at 30 June 2000. There are no material compensating balance requirements associated with these facilities.

NOTE 17 LONG-TERM DEBT

	Telecom Group		
	31 March 1999	30 June 1999	30 June 2000
(Dollars in millions)	NZ$	NZ$	NZ$
TeleBonds	401	364	387
Eurobonds	655	655	480
Euro Medium Term Notes	–	–	1,650
Swiss franc issue	150	150	150
Finance leases (see Note 20)	90	87	81
Bank facility	–	–	309
Other loans	6	6	6
	1,302	1,262	3,063
Less unamortised discount	(13)	(12)	(14)
	1,289	1,250	3,049
Less long-term debt maturing within one year (see Note 16)	(177)	(247)	(188)
	1,112	**1,003**	**2,861**
Schedule of Maturities*:			
Due 1 to 2 years (7.58%)	253	177	908
Due 2 to 3 years (8.52%)	221	209	269
Due 3 to 4 years (7.71%)	93	223	137
Due 4 to 5 years (7.90%)	239	89	769
Due over 5 years (8.12%)	306	305	778
Total due after one year (7.85%)	1,112	1,003	2,861

(weighted average effective interest rate for Telecom Group – includes the effect of hedging transactions, see Note 19)*